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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1978

No. 78-295

KORACORP INDUSTRIES INC. and KORATEC COMMUNICATIONS, INC.,
Petitioners,

vs.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

PETITION FOR A WRIT OF CERTIORARI
to the United States Court of Appeals
for the Ninth Circuit

RICHARD J. ARCHER
LEE J. SCLAR
SULLIVAN JONES & ARCHER
Hallidie Building
130 Sutter Street
San Francisco, California 94104
Telephone: (415) 397-7667
Attorneys for Petitioners
Koracorp Industries Inc.
and Koratec Communications, Inc.

PERNAU-WALSH PRINTING CO. - 562 MISSION STREET - SAN FRANCISCO, CA 94105
A BOWNE COMPANY

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Koracorp Industries Inc. ("Koracorp") and Koratec Communications, Inc. ("KCI") respectfully petition for a writ of certiorari to review judgments which the United States Court of Appeals for the Ninth Circuit entered against them in this matter.

OPINIONS BELOW

The opinion of the District Court for the Northern District of California is not officially reported.

The opinion is unofficially reported at [1975-76 Transfer Binder] FED. SEC. L. REP. (CCH) ¶95,532 and is appended hereto as Appendix A. The opinion of the Court of Appeals for the Ninth Circuit is reported at 575 F.2d 692 and is appended hereto as Appendix B.

JURISDICTION

The judgment of the court of appeals was entered February 6, 1978. On May 24, 1978, that court entered an order (attached hereto as Appendix C) denying a timely rehearing petition by Koracorp and KCI. This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

QUESTION PRESENTED

The petitioner corporation discovered misstatements in its filings with the Securities and Exchange Commission, disclosed them to the SEC and the public, cooperated with the SEC to discover those persons responsible, and installed new management. More than two years later, the SEC filed an action against the corporation (and others) to enjoin fraud. Based on undisputed facts as to the corporation—and particularly its conduct since discovery of the misstatements—the district court granted summary judgment in favor of the corporation on the ground that there was no reasonable expectation of future violations. The court of appeals reversed and ordered a pro-

tracted trial on issues relating to the long past misstatements.

The question presented is whether the district court advanced the efficient administration of justice by granting summary judgment after concluding from undisputed facts that there was no reasonable expectation of future violations.

The SEC considers this question of "substantial importance", because it so stated in its application of October 3, 1977, to have extended argument before the Court of Appeals for the Ninth Circuit.

STATUTES AND RULE INVOLVED

This case involves Section 20 of the Securities Act of 1933 (15 U.S.C. § 77t), Section 21 of the Securities Exchange Act of 1934 (15 U.S.C. § 78u) and Rule 56 of the Federal Rules of Civil Procedure. The pertinent portions thereof are reprinted in Appendix D.

STATEMENT OF THE CASE

In November 1975 the SEC filed suit to enjoin allegedly fraudulent conduct by Koracorp, its wholly owned subsidiary KCI, and others.[1] The case arose

[1]The statutes allegedly violated were Section 17(a) of the Securities Act of 1933 (15 U.S.C. § 77q(a)) and Sections 10(b) and 13(a) of the Securities Exchange Act of 1934 (15 U.S.C. §§ 78j(b) and 78m(a)). Jurisdiction was based on Sections 20 and 22 of the Securities Act (15 U.S.C. §§ 77t, 77v) and Sections 21 and 27 of the Securities Exchange Act (15 U.S.C. §§ 78u, 78aa).

from overstatement of KCI accounts receivable in Koracorp reports issued before August 1973. Existence of the lawsuit placed Koracorp under a cloud which affected its executive recruitment and, at least temporarily, the value of its stock. Koracorp and KCI therefore promptly filed a summary judgment motion instead of an answer. The ground for the motion was that events after August 1973 negated any reasonable expectation of future misstatements. Evidence supporting the motion established the following facts:

During the first week of August 1973 Koracorp's board of directors learned that most or all KCI accounts receivable might be uncollectable. On August 7, 1973, Koracorp requested the stock exchanges to suspend trading in Koracorp common stock. Koracorp also informed the SEC, which on August 8, 1973, suspended all trading in Koracorp securities. Almost concurrently Koracorp's board replaced the corporation's president, terminated the vice-president for the division which included KCI, and required KCI's top two officers to resign.

Starting shortly thereafter, Koracorp—led by a new chief executive officer—changed its auditors, restructured its board of directors, and revamped its accounting and legal compliance procedures. Koracorp also disseminated many documents revising and supplementing its pre-August 1973 reports about KCI and the latter's impact on Koracorp operations.

In October 1973 the SEC ordered a formal investigation of Koracorp. Three months later the SEC authorized a resumption of trading in Koracorp securities. By that time the SEC had completed much of its investigation, and after June of 1974 almost no investigation took place.[2] For over two years the SEC received frequent proposed and definitive filings from Koracorp, had repeated communications with Koracorp's counsel, received modified documents complying with each of its comments, and never suggested that any definitive filing failed to make proper disclosure.

The SEC made no effort whatsoever to disprove the above facts. It tried to justify its November 1975 lawsuit with evidence suggesting that Koracorp could have uncovered the true state of KCI receivables earlier than August of 1973. The SEC argued that such evidence, together with Koracorp's admitted misstatements before August 1973, established securities laws violations which should give rise to a never-ending inference of future violations. The SEC also contended that Koracorp's post-August 1973 reporting about KCI was false or misleading in a number of ways.

Koracorp and KCI did not respond to the SEC's version of what transpired before August 1973. They presented no evidence regarding events of that period. They instead detailed uncontradicted evidence show-

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[2]At the time suit was filed the SEC investigation encompassed more than 17,000 documents and extensive sworn testimony from 38 witnesses.

ing a lack of substance in every SEC allegation of a later misstatement; and they explained that the undisputed evidence of events between August 1973 and March 1976 negatived any reasonable implication of future violations from pre-August 1973 happenings.

On March 19, 1976, the district court granted summary judgments to Koracorp, KCI, and certain other defendants. The court acknowledged the "very serious" nature of what happened before August 1973, but said "the question here is whether or not there is reason to believe that they're going to continue". In its opinion of March 26, 1976 (Appendix A hereto), the court ruled that it could not infer "any expectation of future violations, let alone a reasonable one," given the undisputed evidence of events after August 1973.

The court of appeals reversed all judgments except that for Koracorp's former auditor, Arthur Andersen & Co. ("Andersen"). While recognizing that "no violations had occurred for about eighteen months before the district court granted summary judgment" (575 F.2d at 697, App. B at B-7), two judges held as to all defendants other than Andersen that

> "an inference arises from illegal past conduct that future violations may occur . . . Assessing the likelihood of recurrent violations . . . requires the court to probe the defendants' states of mind. Two facts are critical to this inquiry: 'the character of past violations' and 'the bona fides of the expressed intent to comply.'" (575 F.2d at 698-99, App. B at B-9—B-11.)

Those two judges concluded that determination of the two "critical" "facts" required assessment of witness credibility and thus a trial. (575 F.2d at 699, App. B at B-12.) The appeals court majority also lumped Koracorp and KCI into a group of defendants which supposedly admitted evidentiary conflicts as to pre-August 1973 culpability. (575 F.2d at 697, App. B at B-7.) The court ruled that the uncontroverted events after August 1973 could not sustain the summary judgments both because "the district court improperly allocated the burden of persuasion" (575 F.2d at 697, App. B at B-8) and because the post-August events "failed . . . to defeat the SEC's suits as a matter of law" (575 F.2d at 698, App. B at B-10).

The court of appeals' third judge filed a separate opinion in which he objected to a trial because it "could well require months of a district court's time". (575 F.2d at 702, App. B at B-19). In his view, a trial could be avoided "if the district judge assumed as proven the specific charges as set forth in the majority opinion". (575 F.2d at 702, App. B at B-19—B-20.)

REASONS FOR GRANTING THE WRIT

In *United States v. W. T. Grant Co.*, 345 U.S. 629, 633-36 (1953), this Court held that because "an injunction is to prevent future violations"[3] and equity's

[3]The purpose of an injunction under the Securities Act or the Securities Exchange Act is the same. The SEC may obtain an injunction only against a defendant who "is engaged or is about

"discretion is necessarily broad", the government "must satisfy the court that relief is needed" in any lawsuit where it seeks an injunction. The Court further held that in such a suit the district court may grant summary judgment for the defendant if there is no "genuine . . . factual dispute about the existence of . . . [a] significant threat of future violation" and the uncontroverted facts provide a "reasonable basis" for believing future violations unlikely. The Court specifically refused to regard either characterization of a defendant's undisputed past conduct (e.g., negligent, intentionally wrong) or assessment of his future intentions from uncontroverted evidence as factual issues precluding summary judgment.

The Ninth Circuit's decision in this case conflicts with all those holdings. If it is allowed to stand, it will saddle overburdened judges (and defendants) with pointless trials where courts[4] have already concluded that the government's undisputed evidence of past conduct, however characterized, justifies no injunctions in light of other undisputed evidence.[5]

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to engage" in a violation. 15 U.S.C. §§ 77t(b), 78u(e); *SEC v. Commonwealth Chemical Securities, Inc.*, 574 F.2d 90, 99-100 (2d Cir. 1978); see *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 60-61 (1975).

[4]In this equitable action not only was the court the trier of fact, but, also, trial of this case would have been and will be (unless this Court reverses the Ninth Circuit) before the same judge who granted summary judgment (N.D.Cal. Local R. 205-1).

[5]The Ninth Circuit's decision cannot be explained as simply requiring a finding about the character of past conduct. As Koracorp and KCI pointed out in the court below, Rule 52(a) of the Federal Rules of Civil Procedure expressly relieves a district court of any obligation to make findings upon the grant of summary judgment. *See also Helena Rubinstein, Inc. v. Bau*, 433 F.2d 1021, 1024, n.2 (9th Cir. 1970).

1. The Appeals Court Holding That Characterization Of Past Conduct Is A "Fact" Conflicts With Rulings In W. T. Grant.

The principal defendant in *United States v. W. T. Grant Co.* was Hancock, a director in three pairs of competing corporations. According to government complaints, Hancock's three pairs of directorships were corporate interlocks prohibited by Section 8 of the Clayton Act. Soon after suit was filed, Hancock resigned one directorship in each pair, filed affidavits to that effect, and moved for summary judgment. (345 U.S. at 630.) Hancock disclaimed any intent to resume the same interlocks (345 U.S. at 633), but he refused to promise abstention from similar situations or concede his conduct had been illegal (345 U.S. at 634). It was also undisputed that Hancock maintained the interlocks until suit was brought, despite five years of administrative attempts to persuade him of the interlocks' illegality. *(Id.)* With no other evidence before it, the district court granted summary judgment. It ruled that "there is not 'the slightest threat that the defendants will attempt any future activity in violation of § 8 (if they have violated it already). . . .'" (345 U.S. at 631.)

This Court affirmed. It did so notwithstanding both Hancock's refusal to concede past illegality and the district court's above quoted eschewal of a legal characterization for the past conduct. The Court expressly noted the ambiguous character of Hancock's conduct during the five years of administrative persuasion, saying such past conduct "could easily sup-

port an inference" that Hancock was unsure whether his actions were illegal. (345 U.S. at 634.) The Court nevertheless held that "in these circumstances, the District Judge could decide . . . that there was no factual dispute". (345 U.S. at 635.) By so holding, this Court established that the characterization of undisputed conduct is not a "fact" for summary judgment purposes in an equitable action.

The contrary standard which the Ninth Circuit laid down in this matter must be annulled to prevent waste of trial time; and this Court should effect the annulment here even though the appeals court attributed to each defendant except Andersen an admission of evidentiary conflict regarding events regarding events before August 1973. While an actual concession of factual conflicts between the SEC and Koracorp or KCI might make this case unsuitable for certiorari (though not lessening the case's undesirable *stare decisis* impact), the record here simply does not support the existence of any such concession by Koracorp or KCI. Quite the opposite, as Koracorp and KCI pointed out in both their appeals court brief and rehearing petition, "Koracorp and KCI did not dispute the SEC's district court statement of pre-August 1973 facts" anywhere in the summary judgment proceedings. Among Koracorp, KCI, and the SEC, only the SEC presented evidence on events before August 1973.[6] Koracorp and KCI based their

[6]The SEC's substantial presentation of such evidence, its arguments about the importance of that evidence, and the district court's words and actions refute the Ninth Circuit's assertion

summary judgment motion exclusively on later events, and they did not challenge the credibility of testimony in transcripts tendered by the SEC.

Other defendants' factual showings may have conflicted with those of the SEC, but neither such conflicts nor those defendants' admissions of such conflicts[7] could establish any evidentiary conflict between the SEC and Koracorp or KCI. Nor, contrary to an SEC contention on appeal, can any factual dispute between Koracorp and the SEC be conjured out of alleged inconsistencies between Koracorp's "litigation posture" in this case and in others where Koracorp sued some of the defendants to this proceeding. Koracorp's litigation posture in this case is that it made a summary judgment motion without yet taking

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that "at the initial hearing [three months before summary judgment] the district court . . . accepted suggestions by the defendants that the nature of the defendants' [pre-August 1973] activities . . . was not significant . . . . [and] accordingly restricted the inquiry into the conduct of the parties after . . . August, 1973". (575 F.2d at 697, App. B at B-6.) The defense suggestions which the district court accepted were (1) that the court promptly consider motions based "on the ground that even though everything the SEC says [about events before August 1973] is true, there is no need for an injunction now" and (2) that given the SEC's extensive administrative discovery (see n.2, *supra*) an expeditious resolution of those motions could be fairly accomplished with discovery initially limited to events after August of 1973. At the summary judgment hearing the district court showed its consideration of events before August 1973 by describing those events as "very serious".

[7]The court of appeals quoted one brief as saying: "[T]he moving Defendants conceded, in the court below, the existence of conflicts in the evidence concerning culpability in 1973." (575 F.2d at 697, App. B at B-7.) This was a misquotation of language which really began "[T]he Moving Defendants", where "Moving Defendants" had been previously defined in that brief as parties in an appeal (No. 76-2964) separate from that involving Koracorp and KCI (No. 76-2547), although both appeals were argued in one hearing and resolved in one opinion.

any position on who bears what degree of responsibility for events preceding August 1973. Such a posture fails to conflict with Koracorp assertions of fault in other cases let alone with SEC evidence in this case.

The court of appeals should accordingly have sustained the Koracorp and KCI summary judgments even if the district court was required in March 1976 to consider the character of events that occurred before August 1973. The situation was legally indistinguishable from that in *W. T. Grant* where this Court upheld the chancellor's discretion to grant summary judgment despite ambiguity in the character of Hancock's undisputed conduct. The Ninth Circuit's decision denying that discretion to equity courts will be detrimental to the efficient administration of justice and should be reversed.

2. The Appeals Court Holding That Characterization Of Past Conduct Is "Critical" When Subsequent Events "Fail . . . To Defeat Suit . . . As A Matter Of Law" Does Not Accord With W. T. Grant.

This Court held in *W. T. Grant* that the character of past violations is a consideration only "in some cases". (345 U.S. at 633.) The Court ruled that "were we sitting as a trial court . . . [it] might be persuasive" that Hancock kept up his allegedly illegal conduct for five years, ended it only when sued, and refused to concede its illegality, but that the summary judgment for Hancock had to be sustained unless "there was no reasonable basis for the District Judge's decision". (345 U.S. at 634.) The Court found a "reasonable basis", despite the unresolved

legal character of Hancock's past conduct, because "a proclivity to violate the statute need not be inferred" from that conduct and because the five year "postponement of suit indicate[d] doubt on the prosecutor's part". *(Id.)* The significance of Hancock's claimed intent to refrain from the same interlocks but not necessarily from similar ones and the amount of contrition Hancock should be expected to show were, held this Court, "addressed to the discretion of the trial court". *(Id.)*

> "The necessary determination is that there exists some cognizable danger of recurrent violation, something more than the mere possibility which serves to keep the case alive. The chancellor's decision . . . is necessarily broad and a strong showing of abuse must be made to reverse it." (345 U.S. at 633.)

W. T. Grant thus authorizes summary judgment without characterization of a defendant's uncontested past conduct if the government's actions and the defendant's subsequent behavior are established by undisputed evidence and that evidence can support rational disbelief in the likelihood of future wrongdoing. That standard cannot be reconciled with the test which the Ninth Circuit created in this case, since the latter precludes summary judgment absent either a "critical" stipulated characterization of past conduct or undisputed subsequent events that "defeat the [government's] suit as a matter of law". This case exemplifies the conflict in the two rulings. Although Koracorp and KCI made no stipulation about

the character of their pre-August 1973 conduct, the undisputed evidence of ensuing events shows that the district court had a reasonable, if not compelling, basis for concluding that those defendants posed no cognizable danger of future violations.

The most obvious factor supporting the district court's conclusion is the SEC's wait from August 1973 until November 1975 to bring this suit. That lapse of time implies doubt about the need to enjoin Koracorp and KCI, just as the long delay in suing Hancock "indicate[d] doubt" on the government's part in *W. T. Grant*. The delay is especially significant in this case for three reasons. First, "Congress . . . has concluded that 10 days is sufficient for gathering necessary evidence" about possible securities laws violations. *SEC v. Sloan*, ... U.S. ....., ..., 98 S.Ct. 1702, 1710 (1978). Second, at least until this year, the SEC imposed successive ten day suspensions on trading of a security whenever the SEC felt that was "require[d] . . . to maintain orderly and fair capital markets" (*id.*, quoting SEC brief), yet in January 1974 the SEC lifted a five month series of trading bans on Koracorp securities.[8] Third, the SEC did not dispute that in the two years preceding summary judgment it received all requested changes in proposed Koracorp filings while not suggesting a lack of proper disclosure in any definitive filing until its November

[8]The SEC's position in *Sloan, supra,* shows that termination of the trading bans was significant even though accompanied by a pro forma SEC notice not to equate resumed trading with full public disclosure by Koracorp. *Cf., McConnell v. Lucht,* 320 F.Supp. 1162, 1166 at nn. 6, 7 (S.D.N.Y. 1970) (SEC approval of proxy materials).

1975 lawsuit alleged Koracorp misstatements up to that date. *Cf., e.g., SEC v. Sorg Printing Co., Inc.*, [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶95,034 at 97,614-15 (S.D.N.Y. 1975); *Scott v. Multi-Amp Corp.*, 386 F.Supp. 44, 73 (D.N.J. 1974).

A related basis for summary judgment was Koracorp's securities laws compliance after August 1973. The district court held that the undisputed facts showed no violations for at least eighteen months before its decision (App. A at A-2), and the court of appeals agreed (575 F.2d at 697, App. B at B-7).[9] Such a long period free of violations is well recognized as belying the need for an injunction. *SEC v. Parklane Hosiery Co., Inc.*, 422 F.Supp. 447, 486 (S.D.N.Y. 1976) (one and one-half years), *aff'd*, 558 F.2d 1083, 1089-90 (2d Cir. 1977); *SEC v. Keller Industries, Inc.*, 342 F.Supp. 654, 660 (S.D.N.Y. 1972) (three years).

Changes in personnel and procedures also support a determination that no injunction is needed. *E.g., SEC v. Cenco, Inc.*, 436 F.Supp. 193, 200 (N.D.Ill. 1977); *SEC v. Keller Industries, Inc., supra*, 342 F.Supp. at 660. Undisputed Koracorp evidence

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[9]Since the appeals court did not accept an SEC assertion of evidentiary conflicts concerning Koracorp disclosure after August 1973, this petition does not address that assertion. The record would show, if examined, that arguments about Koracorp compliance following August 1973 involved no dispute as to any material fact. SEC arguments about subsequent Koracorp compliance were on a par with SEC arguments about subsequent Andersen disclosure. The Ninth Circuit aptly described the latter as "hard to follow" and lacking "any significance . . . [to] a reasonable shareholder". (575 F.2d at 700-01, App. B at B-15, B-17.)

showed such changes after 1973. While the SEC argued about the significance of those unchallenged facts, the question of whether they showed the corporation's bona fide intention to comply with the law was "addressed to the discretion of the trial court" (*W. T. Grant,* 345 U.S. at 634).

The Ninth Circuit holding that only trial can determine the bona fides of a past wrongdoer's expressed intent to comply with the law is plainly inconsistent with the above quoted discretion which *W. T. Grant* vests in equity judges on undisputed facts. Even on the Ninth Circuit's assumption that uncorroborated, self-serving assertions are the sole evidence of intent (575 F.2d at 699, App. B at B-12), that court's position is inconsistent with this Court's ruling in *W. T. Grant* that summary judgment could be partially based on Hancock's limited disclaimer regarding his future intentions. Certainly, the Ninth Circuit's decision tying intent to a trial of witness credibility is erroneous and irreconcilable with *W. T. Grant* when, as in this case, the evidence presented about a corporation's intentions is not hedged promises but sworn and undisputed proof of new personnel and procedures and extended compliance with the law. This Court should reverse the Ninth Circuit's trial-wasting decision and reaffirm its own holding in *W. T. Grant* that when the material facts (including a long delay in bringing suit) are uncontroverted and provide a rational basis for denying an injunction, then an equity court is entitled to exercise its discretion without trial and grant summary judgment for

the defendant even though the defendant's undisputed past conduct lacks an agreed characterization and the other undisputed facts do not compel rejection of the government's petition.

3. The Appeals Court Decision Making Defendants Bear The Burden Of Persuasion, Notwithstanding Undisputed Facts, Conflicts With W. T. Grant.

Another ground which the Ninth Circuit gave for reversing the Koracorp and KCI summary judgments was that "the district court improperly allocated the burden of persuasion". (575 F.2d at 697, App. B at B-6.) The court of appeals said:

> "The burden was upon the KCI and Koracorp defendants, as the parties moving for summary judgment, clearly to establish the non-existence of any genuine issue of fact material to judgment in their favor. (6 Pt. 2 J. Moore, *Federal Practice* ¶56.15[4], p. 56-511.) In granting these defendants' motions for summary judgment, the district court erroneously reversed the burden, stating, '[i]n attempting to meet its burden of showing a reasonable expectation of further violations, the SEC seemed more concerned with creating a factual pattern which would thwart the motion for summary judgment than establishing hard facts on which such an expectation could be asserted.' " (575 F.2d at 697-98; App. B at B-8.)

The appeals court thereby so muddled the burden of persuasion on uncontroverted evidence with the burden of establishing an absence of material fact disputes that it contravened the holdings in *W. T. Grant*

which make the government "satisfy the court that [injunctive] relief is needed"[10] (345 U.S. at 633) and leave that burden unchanged in a summary judgment proceeding where material facts are undisputed (345 U.S. at 633-36).

As shown in Sections 1 and 2 above, the summary judgment proceeding in this case involved no material fact dispute between the SEC and Koracorp or KCI. The Ninth Circuit could not properly manufacture such a conflict by quoting out of context a district court reference to "the SEC . . . creating a factual pattern which would thwart . . . summary judgment". In the full text of the district court's opinion, that "factual pattern" is clearly seen as an objectionable SEC effort to prolong this litigation by citing to "*purported* 'facts in dispute' " rather than "establishing *hard* facts" in conflict with "the *actual* facts not in dispute". (App. A at A-2 (emphasis added).) Even the court of appeals rejected the unsubstantiated allegations and trivia with which the SEC tried to obscure the significant, undisputed facts showing extended securities law compliance after August 1973. (See text at n.8, *supra*, and accompanying footnote.) The district court was accordingly correct to give the SEC the single "burden of showing a reasonable expectation of further violations". The Ninth Circuit's

[10]The Second Circuit has recently applied that holding in a suit brought by the SEC. *SEC v. Coven*, [Current] FED. SEC. L. REP. (CCH) ¶96,462 at 93,682, n.18 (1978), citing a lengthy discussion in *SCM Corp. v. FTC*, 565 F.2d 807, 812-13 (2d Cir. 1977), of the distinction drawn in *W. T. Grant* between a defendant's burden of showing mootness and the government's burden of demonstrating the need for an injunction.

reversal of that ruling creates a precedent in conflict with *W. T. Grant.*

Exacerbating that erroneous holding is the Ninth Circuit's additional ruling that "an inference arises from illegal past conduct that future violations may occur" (575 F.2d at 698, App. B at B-9). This Court specifically decided in *W. T. Grant* that "an individual proclivity to violate the statute need not be inferred" in all cases of past violations. (345 U.S. at 634.) Indeed, this Court has held that facts which standing alone might sustain an inference requiring trial will not defeat summary judgment even in an action at law if those facts are overwhelmed by others negating the inference. *First National Bank of Arizona v. Cities Service Co.*, 391 U.S. 253, 277, 279-80, 288 (1968).

Moreover, assuming arguendo that defendants have the burden of persuasion in a summary judgment hearing on undisputed facts,[11] still this Court should not sustain an appellate decision which would require a trial each time equity switched that burden around. The remedy in such a situation should be a district court reconsideration of the undisputed facts, not a trial.

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[11]Although the same district court opinion covered the Andersen, Koracorp, and KCI summary judgments (App. A), the Ninth Circuit made no reference to the burden of persuasion in affirming the judgment for Andersen (575 F.2d at 699-703, App. B at B-13—B-18).

CONCLUSION

This Court has recognized that

> "litigation under Rule 10b-5 presents a danger of vexatiousness different in degree and in kind from that which accompanies litigation in general. . . . [E]ven a complaint which by objective standards may have very little chance of success at trial has a settlement value to the plaintiff so long as he may prevent the suit from being resolved against him by dismissal or summary judgment. The very pendency of the lawsuit may frustrate or delay normal business activity of the defendant which is totally unrelated to the lawsuit." *Blue Chip Stamps v. Manor Drug Stores,* 421 U.S. 723, 739-40 (1975).

Those holdings are as applicable in government suits, such as this, as in private cases, such as *Blue Chip Stamps.* The SEC is not above being "flagrantly abusive". *SEC v. Sloan, supra,* ..... U.S. at ....., 98 S.Ct. at 1714 (Brennan, J. concurring).

In this case the district court adopted a reasonable procedure to clear away the cloud created by the SEC suit. That court understood that a 1976 trial would serve no useful purpose, since the undisputed evidence of Koracorp reforms and SEC dawdling after August of 1973 left the court unwilling to infer a likelihood of future misreporting from the undisputed SEC evidence of events preceding that date. The entry of summary judgment in those circumstances was authorized by this Court in *United States v. W. T. Grant Co.*

The Ninth Circuit's reversal shows inadequate appreciation of equity's vast discretion in assessing the need for an injunction to prevent future wrongdoing. The Ninth Circuit decision cannot be reconciled with *W. T. Grant*, where this Court upheld summary judgment on undisputed facts despite the unsettled character of defendant's past conduct and the need to assess his future intentions from limited promises of reformation. The Ninth Circuit decision also conflicts with this Court's holding that the government must satisfy the district judge of the need for an injunction.

This case exemplifies the untoward results which the appeals court decision will cause unless this Court reverses. After Koracorp and KCI answer the SEC's complaint, the district court, defendants, and the SEC will have months of expensive trial about events before August of 1973; and then the district court will restate its already known belief that later events preclude any reasonable inference of future violations. Only a writ of certiorari can prevent such waste in this and similar government lawsuits.

Further, the SEC, more than any other governmental agency, is in a position to coerce consent decrees from defendants. Corporations facing litigation as to past matters must continuously seek favorable discretionary administrative action from the SEC. Rather than risk disfavor with the agency, many corporations take consent decrees. Therefore,

this Court should exercise its reviewing power to sustain district court actions which limit extended trials and coercive action by that administrative agency.

Dated: August 21, 1978.

Respectfully submitted,

RICHARD J. ARCHER
LEE J. SCLAR
SULLIVAN JONES & ARCHER
Attorneys for Petitioners
Koracorp Industries Inc.
and Koratec Communications, Inc.

By LEE J. SCLAR

(Appendices Follow)

Appendices

Appendix A

In the United States District Court
for the Northern District of California

No. C-75-2515 SW

Securities and Exchange Commission,
Plaintiff,
vs.
Koracorp Industries, Inc., et al.,
Defendants.

[Filed March 26, 1976]

MEMORANDUM

The parties in this action appeared before this court on Friday, March 19, 1976, on motions for summary judgment made by defendants Koracorp, Koratek [*sic*], Arthur Andersen & Co., Arthur Cunningham and Jere Helfat. This court ruled at that time, based upon all of the papers filed in this matter and upon the oral arguments then presented to the court, that the summary judgments should all be granted. The other motions pending were not reached.

The parties asked for a written memorandum in this matter embodying the court's reasons for its decision.

To procure an injunction for prospective relief against a party charged with violations of the securi-

ties laws, the Securities Exchange Commission [*sic*] has a heavy burden to sustain:

> The SEC concedes that it has the "burden to present a strong prima facie case of violation." It may well have done so, but that is not enough. There must also be a showing that there exists a "reasonable expectation of further violations." (*SEC v. Keller Industries*, 342 F.Supp. 654, 660 (S.D.N.Y. 1972).)

In attempting to meet its burden of showing a reasonable expectation of further violations, the SEC seemed more concerned with creating a factual pattern which would thwart the motion for summary judgment than establishing hard facts on which such an expectation could be asserted. The purported "facts in dispute" here related primarily to dissatisfactions the SEC apparently entertains with the degree to which corrections and disclosures, made by the parties in the closing months of 1973 and early months of 1974, were adequate disclosures of what occurred in 1973 and earlier. The actual facts not in dispute clearly show efforts by all of the parties defendant in this lawsuit to eradicate the effects of the past, alleged, violations of the securities laws. There is no showing whatsoever of any violations by these parties in the last 18 months, and no facts have been alleged upon which the court could conclude there is any expectation of further violations, let alone a reasonable one.

An injunction in an SEC action is a drastic remedy, (*Securities Exchange Commission v. Franklin Atlas Corp.*, 171 F.Supp. 711, 718 (S.D.N.Y. 1959),) his-

torically designed to deter, not to punish. *Hecht Co. v. Bowles*, 321 U.S. 321, 329 (1944). Injunctions in SEC actions are "subject to principles of equitable discretion." *Hecht Co. v. Bowles*, 321 U.S. 321, 327 (1944). In the absence of a showing that further violations are to be reasonably expected, this court does not believe any injunction is appropriate. Despite SEC arguments to the contrary, what it seeks is more than a mere prophylactic related to the specific facts of the case. The broad, all-encompassing injunction sought here against any conceivable future violations carries the strong inference that the court believes the defendants *would* violate the law but for the court's intercession, an inference this court believes to be too heavy to place on these defendants on as inadequate a showing as has been made here.

Therefore,

IT IS HEREBY ORDERED that summary judgment in favor of defendant Koracorp, Koratek [*sic*], Arthur Andersen & Co., Arthur Cunningham and Jere Helfat be granted.

DATED: 3-26-76

/s/ Spencer Williams
United States District Judge

Appendix B

United States Court of Appeals
for the Ninth Circuit

Nos. 76-2547
76-2964

Securities and Exchange Commission,
Plaintiff-Appellant,
vs.
Koracorp Industries, Inc., et al.,
Defendants-Appellees.

[Filed Feb. 6, 1978]

Appeal from the United States District Court
for the Northern District of California

OPINION

Before: CARTER and HUFSTEDLER, Circuit Judges, and SMITH,* District Judge.

HUFSTEDLER, Circuit Judge:

The Securities and Exchange Commission ("SEC") brought these two suits to obtain injunctions preventing the defendants from committing future violations of the anti-fraud and reporting provisions of the fed-

*Honorable Russell E. Smith, Chief Judge, United States District Court, District of Montana, sitting by designation.

eral securities laws. The district judge granted defendants' motion for summary judgment. The SEC appeals, contending that since material issues of fact are in dispute, the district court abused its discretion in granting summary judgment. We agree with the SEC with respect to all of the defendants except Arthur Andersen & Co. ("Andersen"). With respect to Andersen, we conclude that there was no genuine dispute as to any material fact, summary judgment was permissible, and the district court acted within the scope of its discretion in denying the injunctive relief sought.

Defendant Koracorp Industries, Inc. ("Koracorp") is a corporation, engaged in a number of business enterprises, whose common stock is publicly traded on the New York and Pacific Coast Stock Exchanges. Defendant Koratec Communications, Inc. ("KCI") was a wholly-owned subsidiary of Koracorp whose principal business was the publication of a controlled-circulation advertising magazine, "Homemaking with a Flair" ("Flair"), which was used for direct mail promotion. Defendant Weil was the president of KCI, defendant Cunningham was a vice president and director of Koracorp, and defendant Helfat was chief executive officer and president of Koracorp.

According to evidence presented by the SEC, Weil was the chief architect of the fraud. Weil's compensation depended in part upon the volume of KCI's business. Weil was able to increase his compensation by causing to be placed and carried on KCI's books millions of dollars of uncollectible and sometimes wholly fictitious, accounts receivable. The SEC claimed that

Weil also used these overbooked receivables to conceal kickbacks that were paid to him by corporations with which KCI did business. KCI's financial statements were consolidated with Koracorp's. When KCI's stack of receivables collapsed, Koracorp had to reverse over five million dollars which had been improperly shown as income on its books.

Defendant Andersen, Koracorp's accounting firm, first became aware of irregularities in KCI's accounts receivable while preparing its audit of Koracorp's 1970 financial statement. Andersen received a poor response from selected KCI customers with whom it attempted to confirm receivables. When its examination of contracts and collections failed adequately to support receivables in the amounts recorded, Andersen insisted that KCI's 1970 reserves for uncollectible accounts be increased, and it furnished Koracorp with critical comments concerning the inadequate documentation of transactions at KCI. In its 1971 and 1972 audits, Andersen again attempted to obtain confirmation for KCI's receivables from its customers, and repeatedly cautioned Koracorp about the deficient control procedures and the inadequate written documentation of transactions at KCI. The SEC produced evidence that the principals of KCI, with the assistance, or at least the passive neglect, of one or more of the principals of Koracorp, tried to cover up the overbooked receivables of KCI. By early May, 1973, the accounts receivable of KCI had grown to almost six million dollars, of which five million dollars was long past due or had never been

billed. Cunningham and Helfat were aware of the receivables debacle, and Helfat directed that an internal investigation be conducted.

Following that investigation, Weil, in early August, 1973, admitted to Helfat that almost all of KCI's 1972 accounts receivable from advertising were uncollectible. Koracorp directed Andersen to conduct a special investigation into the accounts receivable situation at KCI. Andersen learned that substantially all of the 1972 confirmed accounts were now disavowed by customers and that the information obtained during the 1972 audit had been misrepresented. On August 7, Koracorp informed the New York and Pacific Coast Stock Exchanges and the SEC, and on August 8, the SEC suspended all trading in Koracorp's securities. On September 10, 1973, Andersen withdrew its auditor's report on Koracorp's 1972 financial statement. The original 1972 financial statement reported earnings per share of $0.27. After restatement in early 1974, by which time five million dollars of improperly stated income of KCI had been reversed, the 1972 revised financial statement showed a loss of $1.02 per share. Trading in Koracorp's securities was not permitted to be resumed until early 1974.

Meanwhile, at a special Koracorp board of directors' meeting on August 7, 1973, the board was informed by Cunningham of KCI's overstated accounts receivable and by Helfat of Weil's offer to purchase Flair. The board agreed to the sale of Flair to Weil, contingent upon his resignation as president of KCI.

On August 24, 1973, the Koracorp board of directors requested Helfat's resignation as president and director of Koracorp, but retained him as a special consultant at full salary with all fringe benefits. The board also removed Cunningham from his position as vice president, after he refused to resign. Cunningham remained as a director of Koracorp until May, 1975. Both Cunningham and Helfat received bonuses based upon Koracorp's original 1972 earnings of $0.27 per share.

After a two-year investigation, the SEC filed these complaints in November, 1975. The SEC alleged that Weil was directly responsible for overbooking accounts receivable and for diverting funds from KCI by collecting illegal kickbacks from Flair's customers. These kickbacks were made to corporations that he and his wife owned, defendants Western Gateway Corp., Verve, Inc., Associated Graphics, Inc., and Allison Production Affiliates, Inc. The SEC also alleged that Helfat and Cunningham knew about the fraud and participated in the cover-up by failing to disclose to the Koracorp board and to the public their knowledge of the spurious accounts receivable, the illegal kickbacks to Weil, and the other irregularities in KCI.

The SEC contended that Andersen was negligent in its audits of Koracorp and in its failure to uncover the KCI scheme. The SEC did not claim that Andersen did any affirmative acts in connection with violations of the securities laws by the principals of

Koracorp and KCI, nor did it contend that Andersen had any actual knowledge of the fraud or of the reporting irregularities.

The SEC sought injunctions against the ten individual and corporate defendants to prevent their participating in any future violations of the federal securities laws. At the initial hearing before the district court, the court accepted suggestions by the defendants that the nature of the defendants' activities in connection with the violations was not significant in deciding whether injunctions should issue. The court accordingly restricted the inquiry into the conduct of the parties after the exposure of the fraud in August, 1973. The court also limited discovery to post-August, 1973, matters, "so that they [the defendants] can use that as a basis for motions for dismissal or summary judgment."

The SEC and Andersen both filed motions for summary judgment. The remaining defendants also accepted the district court's invitation by filing motions for summary judgment. We reverse summary judgment in favor of the defendants, other than Andersen, because the district court improperly allocated the burden of persuasion on motion for summary judgment, and triable issues of material fact foreclosed judgment in those defendants' favor. We affirm summary judgment for Andersen because no material issues of fact remained in dispute, and the district court did not abuse its discretion in denying injunctive relief against Andersen.

I

Everyone agrees that the manipulation of KCI and Koracorp, the cover-up activities in which these corporations were engaged, and the diversion of funds from KCI in the form of "commissions" or "kick-back" involved serious violations of the securities laws conducted over a period of several years. Everyone also agrees that, after the collapse of KCI and the exposure of the fraud, violations ceased. No violations had occurred for about eighteen months before the district court granted summary judgment to the defendants. Finally, everyone agrees that the evidence presented to the district court concerning the nature and extent of the participation of the various defendants in the violations was sharply conflicting.

Weil, Helfat, Cunningham, Koracorp, and KCI convinced the district court that all of the disputed facts were immaterial because each of them had conceded, solely for the purpose of the summary judgment, that each was potentially liable in some unidentified respect for the violations. The nature of these concessions is aptly described in one of the defendants' briefs: "[T]he moving Defendants conceded, in the court below, the existence of conflicts in the evidence concerning culpability in 1973." In addition to these "admissions," the defendants offered evidence tending to prove reformation, and in some instances changed circumstances, making it unlikely that some of the individuals would re-engage in securities transactions.

The primary purpose of injunctive relief against violators of the federal securities laws is to deter future violations, not to punish the violators. *(Hecht Co. v. Bowles* (1944) 321 U.S. 321, 329.) The central issue, therefore, is whether as a matter of law the district court could conclude that "there was no significant threat of future violation." *(United States v. W. T. Grant Co.* (1953) 345 U.S. 629, 635.) If the nature and extent of the culpability of the several defendants is a material fact, summary judgment must be reversed because culpability was hotly disputed.

The burden was upon the KCI and Koracorp defendants, as the parties moving for summary judgment, clearly to establish the non-existence of any genuine issue of fact material to judgment in their favor. 6 Pt. 2 J. Moore, *Federal Practice* ¶ 56.15 [4], p. 56-511.) In granting these defendants' motions for summary judgment, the district court erroneously reversed the burden, stating, "[i]n attempting to meet its burden of showing a reasonable expectation of further violations, the SEC seemed more concerned with creating a factual pattern which would thwart the motion for summary judgment than establishing hard facts on which such an expectation could be asserted."

The district court could not grant summary judgment unless the defendants were entitled to judgment as a matter of law. "[T]he moving party has the burden of clearly establishing the lack of any triable

issue, although the opposing party would at trial have the burden of proof on a particular issue. It is not the function of the trial court at the summary judgment hearing to resolve any genuine factual issue, including credibility; and for the purpose of ruling on the motion all factual inferences are to be taken against the moving party and in favor of the opposing party, and the appellate court will do likewise in reviewing the trial court's grant of summary judgment. Discretion plays no real role in the grant of summary judgment; the grant of summary judgment must be proper under the above principles or the grant is subject to reversal." (6 Pt. 2 J. Moore, *Federal Practice, supra,* ¶ 56.15[8], p. 56-643.)

An inference arises from illegal past conduct that future violations may occur. (*SEC v. Culpepper* (2d Cir. 1959) 270 F.2d 241; *SEC v. Keller* (7th Cir. 1963), 323 F.2d 397, 402.) The fact that illegal conduct has ceased does not foreclose injunctive relief. (*United States v. W. T. Grant Co., supra,* 345 U.S. at 633; *Los Angeles Trust Deed & Mortgage Exchange v. SEC* (9th Cir. 1960) 285 F.2d 162; *SEC v. Manor Nursing Centers, Inc.* (2d Cir. 1972) 458 F.2d 1082.) Promises of reformation and acts of contrition are relevant in deciding whether an injunction shall issue, but neither is conclusive or even necessarily persuasive, especially if no evidence of remorse surfaces until the violator is caught. (*United States v. Parke, Davis & Co.* (1960) 362 U.S. 29, 48 ("A trial court's wide discretion in fashioning remedies is not to be exercised to deny relief altogether by lightly

inferring an abandonment of the unlawful activities from a cessation which seems timed to anticipate suit.").)[1] Moreover, courts must be particularly skeptical about attaching any significance to contrition under protest. (*E.g., SEC v. Manor Nursing Centers, Inc., supra*, 458 F.2d at 1101.) The changed circumstances of the violator are also relevant in determining whether an injunction shall issue, but neither changing jobs nor deterioration of health, in and of itself, or in combination with the cessation of illegal activities and proclaimed reformation, provides a complete defense to an injunction suit. (*E.g., SEC v. Pearson* (10th Cir. 1970) 426 F.2d 1339.)[2]

When the burden of proof is properly allocated to the defendants and the inferences are drawn against them, it is evident that the uncontroverted facts failed to disclose defenses sufficient to defeat the SEC's suits as a matter of law. Therefore, we turn to the question whether the disputed facts presented

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[1]We are reminded of the wry observation of the Seventh Circuit in rejecting the contention of some securities law violators that no injunction was necessary because they had repented and had no intention of repeating their misdeeds: "They came into court with a contrite heart and with the intention to forget and forgive if the Government would meet them half way." (*American Safety Table Co. v. Singer Sewing Machine Co.* [*sic*] (1938) 95 F.2d 543 [*sic*], 553.)

[2]Of course, there are circumstances in which any opportunity to repeat past violations is so remote that summary judgment may be proper. For example, in *SEC v. Penn Central Co.* (E.D.Pa. 1976) 425 F. Supp. 593, a defendant who was partially paralyzed by an acute stroke and who suffered other serious physical disabilities was granted summary judgment. The precarious state of his health made his re-entry into the securities field too remote, as a matter of law, to warrant the issuance of an injunction against him.

triable issues. The nature and extent of the culpability of the several defendants are material. Assessing the likelihood of recurrent violations of the securities laws requires a prediction of future conduct, and that, in turn, requires the court to probe the defendants' states of mind. Two facts are critical to this inquiry: "the character of past violations" and "the bona fides of the expressed intent to comply." (*United States v. W. T. Grant Co., supra,* 345 U.S. at 633. *See also SEC v. National Student Marketing Corp.* (D.D.C. 1973) 360 F. Supp. 284, 297.) As Professor Loss points out: "The ultimate test is whether the defendant's past conduct indicates—under all of the circumstances and not merely in view of the time which has elapsed since the last violation—that there is a reasonable likelihood of further violations in the future." (3 Loss, *Securities Regulation* (2d ed. 1961) at 1976.)

Neither the character of a defendant's past violations nor the bona fides of an expressed intent to comply can be ascertained without determination of the acts and conduct of each of these defendants in connection with the securities violations. An admission that illegal acts occurred for which someone had responsibility, perhaps a little bit of which might be attributed to a particular defendant, provides no clue to any defendant's state of mind for use as a predictor of his future conduct. An exploration of the nature and quality of the conduct of each defendant cannot be avoided by "admissions" that violations occurred for which responsibility need not be allocated.

One or more of these defendants was responsible for gross fraud, for diversion of corporate funds, and for active cover-up of the misdeeds. The allocation of responsibility depends heavily upon the credibility of the testimony of the several defendants. The courts have long recognized that summary judgment is singularly inappropriate where credibility is at issue. Only after an evidentiary hearing or a full trial can these credibility issues be appropriately resolved. (*See, e.g., Poller v. Columbia Broadcasting System, Inc.* (1962) 368 U.S. 464, 473; *United States v. Perry* (9th Cir. 1970) 431 F.2d 1020, 1022; 10 C. Wright & A. Miller, *Federal Practice and Procedure* § 2726 (1973). *Accord* Note of the Advisory Committee on Amended Rule 56 ("Where an issue as to a material fact cannot be resolved without observation of the demeanor of witnesses in order to evaluate their credibility, summary judgment is not appropriate.") 31 F.R.D. 648 (1963).)

The general rule proscribing summary judgment where credibility is in question is particularly pertinent here. Defendants assert that they are now reformed and will never violate the securities laws again. The promises of defendants to obey the law and not to re-enter the securities market are, of course, expressions of the defendants' states of mind and are relevant to a determination of the likelihood of repetition. These statements are, however, necessarily self-serving and highly dependent on the credibility of the individuals making the statements. The fact that illegal conduct ceased provides no fur-

ther support for defendants' assurances that injunctive relief is unnecessary where the acts of contrition and process of reformation did not begin until the defendants must have realized that the accounts receivable scandal could no longer be kept hidden. (*Cf. United States v. Parke, Davis & Co., supra,* 362 U.S. 29, 48.) On this record, the district court could not decide that these defendants, or any of them, would not be recidivists.[3]

II

Summary judgment in favor of Andersen arose in a different context. Both the SEC and Andersen filed motions for summary judgment, each contending that it was entitled to judgment and that there were no genuine issues of fact. The SEC charged Andersen with simple negligence in the pre-August, 1973, period by reason of its failure to uncover the receivables fraud and with willful failure to disclose to the public the details of the KCI receivables fraud during the post-August, 1973, period, during the course of Andersen's special investigation.

The facts surrounding Andersen's audits of Koracorp's financial statements in the years 1970 through 1972, its special investigation in 1973, and its 1974 audit work on Koracorp's restated 1972 financial statement are not controverted. Andersen's statement

[3]We, of course, express no views on the ultimate merits of the case. Nothing we have said should be read as implying a direction to the district court about the appropriate balancing of equities in the issuance or refusal to issue an injunction once the factual issues in dispute have been resolved.

of facts on its motion for summary judgment was adopted by the SEC in its brief in support of its own motion before the district court. The SEC's statement of undisputed facts was likewise not controverted by Andersen.

Upon the basis of these facts, Andersen, solely for the purpose of summary judgment, conceded that the firm's failure to uncover the receivables fraud was due to simple negligence. The SEC accepted that concession as to Andersen's pre-August, 1973, activities. The SEC, however, also claimed that Andersen was guilty of willful failure to disclose to the public details of the KCI receivables fraud during the period from August, 1973, to February 28, 1974.

We first address the question whether Andersen's failure to disclose to the public its findings as it pursued its special investigation was a violation of the federal securities laws. It is uncontested that Andersen along with Koracorp informed the New York and Pacific Coast Stock Exchanges and the SEC of the overbooking of accounts receivable on August 8. Although Andersen had not completed its special investigation in September, Andersen advised the SEC that it was withdrawing its consent to the use of its prior auditor's report in connection with Koracorp's 1972 financial statement, and it confirmed its understanding that Koracorp would "notify the Securities and Exchange Commission forthwith and . . . promptly make appropriate disclosure to the public and to the New York Stock Exchange." In the interim, the SEC had suspended all trading in

Koracorp's securities. Commencing in October, 1973, the SEC began its own extensive investigation of the Koracorp problems. The SEC deposed all of the key Andersen personnel involved in the Koracorp audits, obtained production of documents, including Andersen's work papers, memoranda, correspondence, and reports relating to those audits. Andersen and its personnel voluntarily cooperated with the SEC's investigation both as to document production and deposition testimony.

The SEC's argument that Andersen violated some kind of duty in reporting its findings during its special investigation is hard to follow. As nearly as we can ascertain, its claim of misconduct rests upon a contention that, in Andersen's September 10, 1973, letter to Koracorp and the SEC, withdrawing its consent to the use of its report on Koracorp's 1976 [*sic*] financial statement, Andersen was too cautious in its language. The Andersen letter stated that the information it had obtained "indicates the possibility that the consolidated financial statements of Koracorp Industries, Inc. for the year ended December 29, 1972, may require adjustments," and that "significant amounts of accounts receivable of that subsidiary (KCI) may have been included in these financial statements erroneously. . . ." The SEC argues that Andersen was engaged in a cover-up because it did not then and there state that "egregious management fraud had occurred." The SEC cites no authority and we have found none that poses a duty upon an accountant in the middle of a special investigation

to make a public announcement that the company whose affairs it is investigating is guilty of fraud. There was nothing in the record before the district court which permitted an inference that, under the circumstances of this case, Andersen was guilty of any kind of concealment. Moreover, there is nothing in the record suggesting that the alleged failure to disclose was material to investors. The fact of fraud had been revealed, even if it was not presented in language that the SEC might have chosen. Trading in Koracorp had been suspended for a month preceding Andersen's letter and remained suspended for another five months.

The only other fact to which the SEC points to support its contention that Andersen was guilty of a kind of culpable non-disclosure is that Andersen's February 28, 1974, report on Koracorp's restated 1972 financial statement said that "sufficient information is not available at present to determine the amount of the adjustment relating to this discontinued operation which may be applicable to periods prior to 1972." But the SEC points to nothing that casts any doubt about the accuracy of that statement. The SEC argues that the statement was misleading because it did not also tell investors either how or why the KCI receivables were improperly booked. Perhaps there may be situations in which a failure to report results of an ongoing investigation in greater detail may be misleading, but the record in this case does not support the inferences that the SEC asks us to draw. The SEC has not given us any reason why

there was a substantial likelihood that a reasonable shareholder in 1974 would consider the omitted details of any significance. (*See TSC Industries, Inc. v. Northway, Inc.* (1976) 426 U.S. 438, 448-49.) By 1974 Andersen had already audited Koracorp's year-end 1973 report, trading in Koracorp had been suspended, and there had been substantial public disclosure with respect to the KCI scandal.

We are left then with the SEC's claim that Andersen's failure to detect the overbooking scheme before August, 1973, constituted simple negligence for which injunctive relief would be appropriate.[4]

Unlike the Koracorp and KCI defendants, Andersen's conduct in these transactions was fully exposed, and its state of mind was not in issue. No triable issue of fact remained, as both the SEC and Andersen agreed below. The record thus presented to the district court on the cross-motions for summary judgment the issues: (1) Is injunctive relief under Section 10(b) and Rule 10b-5 available to the SEC against an independent auditor who was guilty of simple negligence, and (2) if the relief is available, did the district court abuse its discretion in refusing to grant injunctive relief?

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[4]The SEC also argues on appeal that Andersen's failure to uncover the fraud was reckless. That contention, however, was not made before the district court, and we, therefore, decline to consider it on appeal. Reliance upon simple negligence, of course, was understandable because at the time the issue was presented to the district court, no shadow had been cast upon *White v. Abrams* (9th Cir. 1974) 495 F.2d 724, holding that, even in private actions, negligence could be a basis for liability.

We need not reach the first question, which was specifically left open in *Ernst & Ernst v. Hochfelder* (1976) 425 U.S. 185, 194 n.12, on this appeal because, even if we assume that simple negligence is enough to sustain the SEC's suit for an injunction, the district court was nevertheless free to exercise its discretion in denying equitable relief against Andersen. No *per se* rule requiring the issuance of an injunction upon the showing of past violation exists. (*SEC v. Bausch & Lomb, Inc.* (2d Cir. 1977) 565 F.2d 8, 18; *SEC v. Management Dynamics, Inc.* (2d Cir. 1975) 515 F.2d 801, 807.) The critical issue is whether there is a reasonable likelihood that the wrong would be repeated. The district court has a significant degree of latitude in making that determination. "[T]he court always is free to direct the entry of summary judgment for defendant where there are no genuine issues of material fact and the court is unwilling to award plaintiff discretionary relief." (10 C. Wright & A. Miller, *Federal Practice and Procedure, supra,* § 2731, at p. 605.) The SEC has failed to show that the district court abused the discretion accorded it. (*SEC v. Bausch & Lomb, Inc., supra,* 565 F.2d at 18.) Although we might have reached a different conclusion if we were sitting as a district court, we cannot say that the district court abused its discretion in declining to issue an injunction against Andersen.[5]

Judgment in favor of Andersen is affirmed. The judgments in favor of the remaining defendants are

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[5]Nothing we have said suggests that we have expressed any view upon the liability, if any, of Andersen for common law negligence.

reversed and the causes are remanded to the district court for further proceedings consistent with the views herein expressed.

JAMES M. CARTER, Circuit Judge, concurring:

I am disturbed by the fact that the majority sends this case back for evidentiary hearings to a busy district court (the Northern District of California at San Francisco) apparently to find specifically the extent of each individual defendant's bad conduct and what his responsibility was in the overall picture. An evidentiary hearing to ascertain the various misdeeds and responsibility of each defendant in connection therewith could well require months of a district court's time. The same issues are present in civil actions pending against these defendants. In some way extensive evidentiary hearings in this case ought to be avoidable on remand to the district court.

The record shows that the individual defendants made admissions that violations occurred, but did not take any responsibility for particular violations (see majority opinion, *supra,* 575 F.2d 699). In view of the pending civil suits against these defendants it is understandable that they are unwilling to make further admissions as to their complicity in the overall scheme. However, perhaps they could make more specific admissions for the purpose of this motion only. Or perhaps the district judge on his own could explicitly assume that the charges by the S.E.C. against each defendant were proven. I think that if the individual defendants admitted for the purposes

of this motion only, or if the district judge assumed as proven, the specific charges as set forth in the majority opinion (575 F.2d 696), then there would no longer be a genuine issue as to any material fact. Summary judgment could then be entered without need of a long evidentiary hearing.

Appendix C

United States Court of Appeals
for the Ninth Circuit

Nos. 76-2547
76-2964

Securities and Exchange Commission,
Plaintiff-Appellant,
vs.
Koracorp Industries, Inc., et al.,
Defendants-Appellees.

[Filed May 24, 1978]

ORDER

Before: CARTER and HUFSTEDLER, Circuit Judges, and SMITH,* District Judge

The petitions for rehearing are DENIED.

*Honorable Russell E. Smith, Chief Judge, United States District Court, District of Montana, sitting by designation.

Appendix D

STATUTES AND RULE INVOLVED

SECTION 20(b) OF THE SECURITIES ACT OF 1933
15 U.S.C. § 77t(b)

Whenever it shall appear to the Commission that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation of the provisions of this title, or of any rule or regulation prescribed under authority thereof, it may in its discretion bring an action in any district court of the United States, United States court of any Territory, or the United States District Court for the District of Columbia to enjoin such acts or practices, and upon a proper showing a permanent or temporary injunction or restraining order shall be granted without bond. The Commission may transmit such evidence as may be available concerning such acts or practices to the Attorney General who may, in his discretion, institute the necessary criminal proceedings under this title. Any such criminal proceeding may be brought either in the district wherein the transmittal of the prospectus or security complained of begins, or in the district wherein such prospectus or security is received.

SECTION 21(d) OF THE SECURITIES EXCHANGE ACT OF 1934
15 U.S.C. § 78u(d)

Wherever it shall appear to the Commission that any person is engaged or is about to engage in any acts or practices constituting a violation of any provision of this title, the rules or regulations there-

under, the rules of a national securities exchange or registered securities association of which such person is a member or a person associated with a member, the rules of a registered clearing agency in which such person is a participant, or the rules of the Municipal Securities Rulemaking Board, it may in its discretion bring an action in the proper district court of the United States, the United States District Court for the District of Columbia, or the United States courts of any territory or other place subject to the jurisdiction of the United States, to enjoin such acts or practices, and upon a proper showing a permanent or temporary injunction or restraining order shall be granted without bond. The Commission may transmit such evidence as may be available concerning such acts or practices as may constitute a violation of any provision of this title or the rules or regulations thereunder to the Attorney General, who may, in his discretion, institute the necessary criminal proceedings under this title.

PARAGRAPHS (b) AND (c) OF RULE 56 OF THE FEDERAL RULES OF CIVIL PROCEDURE

(b) A party against whom a claim, counterclaim, or cross-claim is asserted or a declaratory judgment is sought may, at any time, move with or without supporting affidavits for a summary judgment in his favor as to all or any part thereof.

(c) The motion shall be served at least 10 days before the time fixed for the hearing. The adverse party prior to the day of hearing may serve opposing

affidavits. The judgment sought shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law. A summary judgment, interlocutory in character, may be rendered on the issue of liability alone although there is a genuine issue as to the amount of damages.